National Retail Federation
The Voice of Retail Worldwide

Submission of the National Retail Federation

to the

Select Revenue Measures Subcommittee

of the

House Ways and Means Committee

Hearing

on

Certain Expiring Tax Provisions

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The National Retail Federation (NRF) submits the following comments in conjunction with the April 26 Select Revenue Measures Subcommittee hearing on "Certain Expiring Tax Provisions." In particular, the NRF offers comments in support of retroactively extending provisions relating to the 15-year depreciable life for leasehold, retail and restaurant improvements, and the work opportunity tax credit (WOTC).

The NRF strongly supports Chairman Camp's goal of corporate tax reform that broadens the tax base and substantially lowers the corporate tax rate. In the context of fundamental tax reform, we recognize that all so-called "tax expenditures" will be evaluated and may be eliminated in exchange for substantially lower rates in order to provide a more economically efficient tax system. However, tax reform will take some time to accomplish, and until that occurs, it is important to maintain certain tax provisions that help to stimulate investment and jobs. These provisions need to be extended as expeditiously as possible to eliminate business uncertainty that is causing delays in investment and hiring.

As the world's largest retail trade association and the voice of retail worldwide, NRF represents retailers of all types and sizes, including chain restaurants and industry partners, from the United States and more than 45 countries abroad. Retailers operate more than 3.6 million U.S. establishments that support one in four U.S. jobs – 42 million working Americans. Contributing $2.5 trillion to annual GDP, retail is a daily barometer for the nation's economy.

Depreciation of Leasehold, Retail, and Restaurant Improvements

The existing 39-year recovery period for real estate grossly overstates the useful life of structures and, even more so, the improvements made to structures, increasing the cost of capital and slowing down investment. Studies conducted by the Treasury Department[1], Congressional Research Service[2] and private economists[3] all found that the depreciation life for buildings is too long and that the depreciation life for building improvements is even worse. In fact, tax depreciation rules for investment in nonresidential structures may be the only type of investment where tax rules provide for decelerated cost recovery. As a result, current depreciation allowances generate high tax costs for these investments and reduce investment in these projects.

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[1] *Report to the Congress on Depreciation Recovery Periods and Methods,* Washington, D. C.: U.S. Department of the Treasury, July 2000.
[2] Jane G. Gravelle, *Depreciation and the Taxation of Real Estate,* Congressional Research Service, The Library of Congress, Washington, D.C.: May 5, 1999.
[3] See, for example, Deloitte and Touche, LLP., *Analysis of the Economic and Tax Depreciation of Structures.* Washington, D. C., June 2000.

In the retail trade sector of the economy, structures and especially their improvements do not last for 39 years. Retailers generally remodel their stores every five to seven years to reflect changes in customer taste and needs. Remodeling is needed to maintain the retailer's customer base and compete with newer stores. Moreover, many improvements, such as interior partitions, ceiling tiles, restroom accessories, paint, etc., may only last a few years before requiring replacement.

A provision to temporarily reduce the depreciable life of *leasehold* improvements from 39 to 15 years was first included in the American Jobs Creation Act of 2004. Under this provision, improvements made to buildings that are leased were depreciated over 15 years, but improvements made to buildings that are owned still had to be depreciated over 39 years. The 2004 Tax Act also allowed improvements to restaurants to be depreciated over 15 years, regardless of whether the restaurant was leased or owned.

Approximately, half of retail stores are leased and about half are owned by the retailer. For retailers that lease their property, the leasehold improvement provision greatly reduced the cost of improvements to their stores. However, the leasehold improvement provision put retailers that own their stores at a competitive disadvantage because they had to continue to write-off store improvements over a 39-year period. Congress resolved this inequity in 2008, when they expanded the depreciation "extender" to allow qualified retail improvements to be depreciated over 15 years, regardless of whether the retailer owns or leases his store.[4]

The 15-year depreciable life for leasehold, retail and restaurant improvement property and new restaurant construction expired at the end of 2011. Investments that are made now must be written off over 39 years. Because this is such a large increase in the cost of improvements, retailers have slowed down making improvements pending a decision from Congress as to whether these provisions will be extended.

Retailers' remodeling provides many additional jobs to the economy. According to the Bureau of Economic Analysis, every $1 million spent in the construction industry creates more than 28 jobs in the overall economy. If the write-off for the cost of improvements is 39 years, rather than 15, it will have a negative impact on a retailer's decision to go forward with their remodeling plans and will cost jobs.

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[4] Unfortunately, when Congress fixed the inequity in the law regarding the ability of store owners to write-off their improvements over 15 years, they added a new inequity in the law. The new provision makes owners of retail stores ineligible for utilizing bonus depreciation for their improvements, but lessees of retail store space are permitted to use bonus depreciation. Again, this discriminates among businesses in the same industry based on whether the store is leased or owned. Hopefully, this inequity can be resolved as part of the extension of the depreciation provision.

Work Opportunity Tax Credit

The NRF supports extension of the Work Opportunity Tax Credit (WOTC). WOTC is an important employment incentive. In the retail industry it has had proven results encouraging hiring among certain classes of individuals that might otherwise face difficulty in gaining employment. It also provides resources for job training that is so important in bringing these targeted classes into the labor market.

Conclusion

Extension of business tax provisions that encourage investment and employment should not be delayed until policymakers complete work on comprehensive tax reform. Business uncertainty that has resulted from Congressional delay in extending these provisions has led to a slowdown in investment and hiring. While we are hopeful that the tax reform debate results in policy that provides a more efficient tax system, by exchanging lower tax rates for many of the incentives in the current tax code, it is critical that the current tax system provide certainty in the interim.

We respectfully urge this Subcommittee to act expeditiously to extend business tax “extenders,” and particularly the 15-year depreciable life for leasehold, retail, and restaurant improvements and new restaurant construction, and WOTC, until tax reform can be enacted.